



PENSIONS COMMITTEE

12 December 2023

Subject Heading:

**SERVICE REVIEW OF THE PENSION
FUND CUSTODIAL & PERFORMANCE
MONITORING SERVICE**

CLT Lead:

**1 October 2022 to 30 September 2023
Kathy Freeman**

Report Author and contact details:

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Policy context:

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Services are reviewed to ensure that the Pension Fund is receiving best value for money and is benefiting from all the services the custodian has to offer

Financial summary:

Costs for the custodial services for the period are met by the Pension Fund

The subject matter of this report deals with the following Council Objectives

Communities making Havering	[X]
Places making Havering	[X]
Opportunities making Havering	[X]
Connections making Havering	[X]

SUMMARY

This report reviews the performance of the Custodial and Performance Measurement services provided by Northern Trust, for the period 1 October 2022 to 30 September 2023.

RECOMMENDATIONS

It is recommended that the Committee notes the views of officers on the performance of the Custodian and makes any comment on the report which it considers appropriate (Table 1 and Section 3 refers).

REPORT DETAIL

1. Background

- 1.1 Northern Trust was appointed to commence Custodial and Performance Measurement Services from 1 October 2019 until the 30 September 2023. A new contract was awarded via a direct award for a further three years commencing on 1 October 2023 and will expire on the 30 September 2026
- 1.2 The Pension Funds within oneSource and the London CIV (LCIV) now share the same custodian. Using a single provider across the LCIV and with other underlying LGPS will benefit from having opportunities for efficiencies e.g. having a single system for the transition process, cost benefits (economies of scale from the full breadth of the LCIV relationship) and reduced operational risk.
- 1.3 This period of review covers the custodial and performance measuring services delivered by Northern Trust for the period 1 October 2022 to 30 September 2023.

2. Review of the Custodian's and Performance Measurement service

- 2.1 The Custodian operate a wide range of functions. This falls into the following main categories:

(a) Investment Accounting and Reporting

The Custodian produces accounting reports that are used for producing the Pension Fund Statement of Accounts and enable the Fund to comply with the International Financial Reporting Standards (IFRS), Statements of Recommended Practice (SORP) and Chartered Institute of Public Finance & Accounting (CIPFA) accounting guidance. These reports are accessed and downloaded from their client portal "passport".

They keep a record of the book costs (valuations) and the holdings in the various asset classes for each of the investment managers' portfolio as well as at the total Fund level.

The Fund also subscribes to Northern Trust's additional specialist accounting reporting service which provides:

- a comprehensive suite of financial accounting reports to help facilitate compliance with SORP and assists the Fund in compiling its accounts and,
- includes completion of the relevant investment sections of the UK Office of National Statistic Returns (ONS), which is a statutory requirement.

(b) Safe Keeping and Custody of assets

This refers to the maintenance of accurate records and certificates of the ownership of stock and ensuring that dividend income and other distributions are received appropriately.

(c) Performance measurement

This is a key part of the investment management process and forms an essential component of the reporting requirements of the Fund. Performance measurement enables the Pensions Committee, Investment Consultants and officers to understand whether the investment objectives of the Fund are being met and if the fund managers are achieving their targeted performance.

Northern Trust produce monthly and quarterly reports which include performance returns versus benchmarks for each manager and for the whole Fund over a number of time periods, extending from one month to inception. These reports enable the Fund to comply with CIPFA guidance "Preparing the Annual Report", which must include investment performance set out for each asset class and fund manager against the benchmarks set for one year, three years and five years.

- 2.2 Services are reviewed annually to ensure that the Fund is receiving best value for money and is benefiting from all the services the custodian has to offer. Monitoring the contract also meets post contract award procedures and ensures services are being delivered in accordance to the contract.
- 2.3 Officers have assessed the service against a set of criteria and adopted the RAG rating method to define Green (Favourable output), Amber (Neutral, may require further monitoring) Red (Unfavourable). Officers have shared the outcome of the service review with Northern Trust, which has been set out in the following table:

Table 1

CRITERIA	ASSESSMENT	Rating
Safe Keeping and Custody of Assets		
It is important that the Pensions Committee and officers have confidence that all assets are secure and properly accounted for.	Officers review the custodians audited System and Organisation Control (SOC1) report produced annually. No concerns were raised in their latest report covering the 12 months to 30 Sept 2022. The Sept 23 report will not be available until approximately 6 months after the period end date.	GREEN: Officers have confidence that the assets are accounted for correctly.
Investment Accounting and Reporting		
It is important that accurate accounting records are maintained and appropriate reconciliations can be made against the Fund's investment managers records.	Officers run detailed reports from the custodian's website using their "passport" tool. These reports are reconciled to individual fund manager reports and any differences investigated. This provides assurances that accurate records are maintained. Officers also use the additional reporting functionality that contributes to reconciling the accounts.	GREEN: Officers are satisfied that accurate accounting records are maintained with no audit issues identified to date.
Prompt and responsive service	Reponses to queries are dealt with promptly.	GREEN: Officers are very satisfied and appreciative of the responsive service
Good communication and support	Officers communicate frequently with the custodian covering general day-to-day operations and to obtain assistance in ensuring investment instructions templates are completed correctly.	GREEN: Communications and support continue to be very satisfactory.
Provision of data for the Office of National Statistics (ONS) Returns	The Fund uses the custodians ONS service and they complete the investment sections within the return and answer/resolve any queries raised by ONS. These have been delivered within the required timescales.	GREEN: Officers are very satisfied with this service

CRITERIA	ASSESSMENT	Rating
Performance Measurement		
It is important that the Pensions Committee and officers understand whether the investment objectives of the Fund are being met and if the fund managers are achieving their targets.	Northern Trust performance measurement service produce monthly and quarterly reports setting out performance returns versus benchmarks for each manager and the whole fund over a number of time periods that cover 1 month, 3 months, 1 year, 3 years, 5 years and inception. Performance reports are available via the custodian's website using the "RADAR" tool.	GREEN Performance reports are received within specified timescales and officers are very satisfied with this service.

3. Conclusion

- 3.1 Officers are satisfied with the provision of safekeeping and custody functions.
- 3.3 Officers are satisfied with the overall investment accounting and reporting functions.
- 3.4 Officers are satisfied with the performance monitoring service.

IMPLICATIONS AND RISKS

Financial implications and risks:

As the Fund's asset pool provider London CIV use Northern Trust as their appointed custodian the Fund benefits from a reduced pricing structure offered for those funds that have assets invested on the London CIV platform.

Upon reviewing reconciliation and year-end processes, management recognised the potential key person risk for reconciling the accounts and decided, for service planning reasons, to expand the current contract to include the custodian's additional Specialist accounting reporting service. This additional service means that the custodian is able to produce the accounts and provide officers with access to the comprehensive suite of financial reports, which will further support the reconciliations of the accounts. Officers used this facility for the first time whilst closing the 2020/21 statement of accounts and confirmed that in-house reconciliations undertaken during the year were accurate

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Northern Trust introduced a new pricing structure applicable from the 1 April 2023, offering a more beneficial pricing structure for the provision of custodial services.

See fee table below for fee breakdown:

Table 2

Fee Breakdown	Oct 19 to Sept 20	Oct 20 to Sept 21	Oct 21 to Sept 22	Oct 22 to Sept 23	Total
	Actual £	Actual £	Actual £	Actual £	Actual £
Custody Fee	29,085	28,127	31,144	25,952	114,308
Accounting Services	0	5,000*	10,013	10,000	25,013
Performance Measurement Fees	23,110	23,849	26,947	33,917	107,823
Total	52,195	56,976	68,104	69,869	247,144

* part year only – this service commenced 1 April 2021

Custody – fees cover transaction charges, administration costs, foreign exchange charges and data for use in ONS submissions.

Accounting Services – production of reports used for producing the Pension Fund Statement of Accounts. This additional service was procured from 1 April 2021

Performance Measurement - fees are applied against each manager's performance data and the index against which it is measured.

There is a risk that the Fund's value could be misstated if poor or incorrect data was provided by the custodian. This is mitigated by frequent reconciliations by the custodian to fund manager records and officer reconciliations. Accounting and reporting information is critical for year-end processes and these need to be produced in a timely manner to ensure accounts can be closed within statutory timeframes.

All custodian and performance measurement fees are met from the Pension Fund.

Officers also carry out reviews of Northern Trust Internal Control reports issued by their external auditor. These reports detail tests undertaken by the auditors, testing their internal control environments and key procedures. No material internal control issues were reported.

Legal implications and risks:

There are no apparent legal implications or risks arising from this report.

Human Resources implications and risks:

The recommendations made in this report do not give rise to any identifiable HR risks or implications that would affect either the Council or its workforce.

Equalities implications and risks:

The Public Sector Equality Duty (PSED) under section 149 of the Equality Act 2010 requires the Council, when exercising its functions, to have due regard to:

- i. the need to eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Equality Act 2010;
- ii. the need to advance equality of opportunity between persons who share protected characteristics and those who do not, and;
- iii. foster good relations between those who have protected characteristics and those who do not.

Note: 'Protected characteristics' are: age, sex, race, disability, sexual orientation, marriage and civil partnerships, religion or belief, pregnancy and maternity and gender reassignment/identity.

The Council is committed to all of the above in the provision, procurement and commissioning of its services, and the employment of its workforce. In addition, the Council is also committed to improving the quality of life and wellbeing for all Havering residents in respect of socio-economics and health determinants

An EqHIA is not considered necessary regarding this matter as the protected groups are not directly or indirectly affected.

BACKGROUND PAPERS

None